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CHARLES ELMORE CROPLEY
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Supreme Court of the United States

OCTOBER TERM 1951

No. 179

OSTERMAN & HUTNER, GOLDMAN SACHS & CO., GRAHAM-NEWMAN CORPORATION, NEWMAN & GRAHAM, and ABRAHAM & CO.,

Petitioners,

against

GUARANTY TRUST COMPANY OF NEW YORK, as Trustee under the First Consolidated Mortgage Deed of The Rio Grande Western Railway Company, dated April 1, 1899, JULIUS KLOSTERMAN, THE CHASE NATIONAL BANK OF THE CITY OF NEW YORK, as Trustee under the Refunding and Improvement Mortgage of The Denver and Rio Grande Western Railroad Company's General Mortgage, dated February 1, 1924, CITY BANK FARMERS TRUST COMPANY, as Trustee under THE DENVER AND RIO GRANDE WESTERN RAILROAD COMPANY'S GENERAL MORTGAGE, dated February 1, 1924, THE DENVER AND RIO GRANDE WESTERN RAILROAD COMPANY, and HAROLD S. BARD,

Respondents.

PETITION FOR WRIT OF CERTIORARI TO THE APPELLATE DIVISION OF THE SUPREME COURT FOR THE FIRST DEPARTMENT OF THE STATE OF NEW YORK.

PHILIP B. JACKSON,
Counsel for Petitioners.

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Respondents.

PETITION FOR WRIT OF CERTIORARI TO THE APPELLATE DIVISION OF THE SUPREME COURT FOR THE FIRST DEPARTMENT OF THE STATE OF NEW YORK AND BRIEF IN SUPPORT THEREOF

Petitioners, Osterman & Hutner, et al., intervenors below, as holders of approximately 20% of the Refunding and Improvement Mortgage Bonds of the Denver & Rio Grande Western Railroad Company, pray that a writ of certiorari issue to review the order of the Appellate Divi-

sion of the Supreme Court of the First Department of the State of New York, entered on the 27th day of February, 1951. Leave to appeal from said order, sought by petitioners, was denied by the Court of Appeals of the State of New York, on June 1, 1951. The order of the Appellate Division affirmed an order of the Supreme Court of the State of New York, entered in the office of the Clerk of the County of New York, on the 14th day of September, 1950, fixing certain allowances and authorizing payment thereof.

Opinion Below

The only opinion below is the opinion of the New York Supreme Court (R. 179), not reported. The order of affirmance of the Appellate Division of the Supreme Court (R. 197) and the order of denial of leave to appeal by the Court of Appeals (R. 203) were without opinion.

The opinion of the New York Supreme Court, denying petitioners' intervention discusses the Federal questions raised by petitioners (R. 185). The order denying intervention was modified on appeal by the Appellate Division of the Supreme Court for the First Department to the extent of granting the application to intervene for the purpose of the appeal (R. 200).

Jurisdiction

The order of the Appellate Division of the Supreme Court for the First Department of the State of New York, was entered on February 27, 1951. The Court of Appeals of the State of New York, by order dated June 1, 1951, denied petitioners' application for leave to appeal to that Court. The jurisdiction of this Court is invoked under Section 1257(3) of the 1948 Revised Judicial Code, Title 28, U. S. C. Sec. 1257(3).

The Federal questions determinative of this case were raised by petitioners' motion to intervene for the purpose of objecting to the applications for allowances and, to the extent necessary, for the purpose of appealing from an order that might be entered granting allowances (R. 18-32). As will be shown, the state courts, in making their decisions, necessarily passed upon the Federal questions and in a manner which conflicts with the decisions of this Court in *Brown* v. *Gerdes*, 321 U. S. 178, and *Leiman* v. *Guttman*, 336 U. S. 1.

Portion of the Constitution and Statutes Involved

The relevant portion of the Constitution is Article I, Sec. 8(4). The statutes involved are Section 1334 of the 1948 Revised Judicial Code, Title 28, U. S. C. and Sec. 77(c)(12) of the Bankruptcy Act, Title 11, U. S. C., Sec. 205(c)(12). The relevant portion of the Constitution and of the Statutes are reproduced in the Appendix hereto (p. A-1).

Questions Presented

In the light of the decisions of this Court in *Brown* v. *Gerdes*, 321 U. S. 178, and *Leiman* v. *Guttmann*, 336 U. S. 1:

When under a plan of reorganization, adopted and approved in a proceeding pending in the Federal Court under Section 77 of the National Bankruptcy Act, it becomes necessary to institute and maintain a subsequent judicial proceeding * and the consummation decree thereafter entered by the Federal District Court requires that allowances for compensation for services to be rendered in such subsequent judicial proceedings be allowed by the District Judge and be paid by the reorganized railroad company, as expenses incurred in connection with the proceedings or the Plan.

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* "The judicial proceedings which must be brought by the Trustee of the First Consolidated mortgage * * *" *R. F. C.* v. *D. & R. G. W. R. Co.*, 328 U. S. 495, 530.

May a state court, in which the parties to the reorganization proceedings have instituted such subsequent proceedings, and may such parties and such reorganized railroad company thereafter, over the objection of bondholders affected, disregard the provisions of such consummation decree, i.e.,

(a) May such parties thereafter apply to such state court for allowances for such subsequent services and may such state court entertain such applications?

(b) May such reorganized railroad company request such state court not to charge such allowances to it but to the proceeds of the collateral affected by such subsequent proceedings?

(c) May such state court fix the amount of such allowances and order the same paid, not by the reorganized railroad company, but by application of such proceeds of the collateral security?

(d) May such parties accept such payment?

Statement

The petitioners are the holders of approximately 20% of the Refunding and Improvement Mortgage bonds of the Denver and Rio Grande Western Railroad Company.

The respondents are, in the main, the Indenture Trustees and their counsel, who represent the holders of three formerly outstanding bond issues of the Denver and Rio Grande Western Railroad Company, the subject of Section 77 reorganization proceedings in the United States District Court for the District of Colorado.

The present issue involves the right of respondents to seek, and the jurisdiction of the New York state court to grant allowances of compensation to respondents and others and to order the same paid out of the proceeds of collateral held by respondents as security for the payment of their respective bond issues. Such compensation was

sought for services rendered in proceedings brought in the State Court by respondents to determine the respective rights of the holders of their three issues of bonds in stock of Utah Fuel Company, pledged, with other collateral to secure payment of the obligations of the railroad company. The Federal Court had previously taken jurisdiction of the collateral in the pending 77 proceedings affecting the railroad and had stayed any action thereon by the respective respondent-trustees.

The plan filed by the railroad company in the 77 proceedings and approved by the Federal Courts had cancelled the liens of the respective bond issues on all collateral except the pledged stock of the Utah Fuel Company; as to that the plan "did not in any way change or affect existing rights in the collateral" * and this treatment necessitated the subsequent judicial proceedings to determine the respective deficiencies and consequent priorities and claims of the bond issues against the Utah Fuel stock.† After this Court so held, the District Court made its consummation decree which provided:

> "The Reorganized Company shall pay to each of said trustees reasonable compensation for services rendered and reimbursement for expenses incurred by it, including attorneys' fees, in securing an adjudication of its interests or claims, if any, as trustees, in and to said stock of the Utah Fuel Company, in such amount as may hereafter be approved and allowed by this Court" (Par. 19, R. 68).
>
> * * * * * *
>
> "The Reorganized Company shall also pay, in such amounts as * * * shall hereafter be allowed by this Court * * * all other expenses and costs of the administration of these proceedings, including allowance of fees or compensation for services and reimbursement of expenses * * * hereafter rendered or incurred in connection with these proceedings or the

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* *R. F. C.* v. *Denver and Rio Grande W. R. Co.*, 328 U. S. 495 530.

† Ante, footnote p. 3.

> Plan by or on behalf of parties to these proceedings * * * all compensation for services rendered and all expenses incurred by the trustees now acting under the mortgages referred to in paragraphs * * * (18) [the mortgages involved in the present suit] of this order which would have been secured, respectively, by the liens of such mortgages, if such mortgages had not been satisfied, cancelled, and released by, or pursuant to, this order, shall be deemed to be expenses incurred in connection with these proceedings or the Plan" (Par. 7, R. 62, 63).
>
> * * * * * * *
>
> "The Court hereby reserves jurisdiction to allow fees or compensation for services and reimbursement for expenses * * * hereafter rendered or incurred in connection with these proceedings or the Plan * * * " (Par. 50, R. 77).

Immediately after the entry of the Consummation Decree, the respondent Trustee of the First Consolidated Mortgage instituted the state court proceedings and, in consequence of a judgment entered therein, the collateral, the Utah Fuel stock, was sold and the proceeds allocated to the respective bond issues in the order of the respective priorities of lien, as found by the state court decree.

After payment to the First Consolidated Mortgage bondholders of the amount of their adjudged deficiency, there remained an overplus of $800,000, which became payable to the Refunding and Improvement Mortgage bondholders, under the terms of the state court findings. However, in lieu of making application for allowances of compensation to the District Judge under the terms of the consummation decree, the respondents, the indenture trustees and their counsel, made application to the state court judge for such allowances of compensation payable from the overplus of the proceeds of sale of the collateral otherwise payable to the Refunding and Improvement Mortgage bonds. The state court judge, over the objection of these petitioners, made an order granting to respondent-trustees and their counsel and to counsel for respondent bondholder-intervenors allowances aggregating $266,427 and the same

were paid by the respondent Trustee for the First Consolidated Mortgage to itself and the other claimants.

From two orders, one denying these petitioners leave to intervene for the purpose of objecting to such allowances and appealing from any order granting the same, and the second, the order granting such allowances, these petitioners appealed to the Appellate Division of the Supreme Court of the State of New York. That Court affirmed the order denying the allowances; it modified the order denying intervention by granting leave to intervene for the purpose of taking the appeal. Application for leave to appeal to the New York Court of Appeals was denied by that Court.

Petitioners urged in the courts below that under Federal Bankruptcy law and the provisions of the Consummation Decree the state court was without jurisdiction to grant allowances and direct a contrary method of payment. The state courts' orders necessarily involved a consideration and rejection of this contention.

Petitioners, having exhausted their state court remedies, now petition this Court for a writ of certiorari to review the order below.

Reasons for Granting the Writ

The determination below in this case constitutes and approves a direct disregard and express violation of

(1) A decree of a Federal Court in a Federal reorganization proceeding, concurred in by the parties thereto, standing unchallenged and unreversed;

(2) The exclusive jurisdiction of the Federal courts:

(a) to control reorganization fees and expenses and

(b) "to police the return which all securityholders obtain from reorganization plans." *

* *Leiman* v. *Guttman*, supra, p. 8.

(3) The determination below is in direct conflict not only with the decisions of this Court but also with the decision of the Federal Court of Appeals for the Third Circuit in *New York Trust Co.* v. *New York & Greenwood Lake Ry. Co.*, 156 F. 2d 701, where comparable and apposite factual and legal situations existed.

ARGUMENT

The Federal jurisdiction to grant compensation under Section 77 and other Federal reorganization statutes and to fix allowances therefor is exclusive.

(*Brown* v. *Gerdes*, supra;
Leiman v. *Guttman*, supra.)

There can be no challenge of the basic fact that by its Consummation Decree,* entered in the reorganization proceeding in which the Federal Court had taken jurisdiction of the *res* and to which jurisdiction the Indenture Trustees and their counsel had submitted fully and unqualifiedly, and in which they had litigated questions respecting the *res* (including the disposition of the collateral, the Utah Fuel stock) †, the Federal Court had

(1) Adjudicated

(a) that the services to be rendered in the subsequent judicial proceedings should be "deemed to be ex-

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* Entered by the Court with the concurrence of these respondents, i.e., the Indenture Trustees, their counsel and the reorganized railroad.

† The Trustee of the First Consolidated Mortgage had applied to and had received from the Federal Court compensation for services in the reorganization proceeding and expressly in connection with the proposals respecting the Utah Fuel Collateral (242 ICC 629, 640, 641).

penses incurred in connection with these proceedings or the Plan" (Decree, Par. 7, R. 63);

(b) that allowances of compensation for the subsequent judicial proceedings should be "approved and allowed by (it) this Court" (id., Par. 19, R. 68);

(c) that the "Reorganized Company shall pay to each of said trustees reasonable compensation * * * including attorneys' fees, in securing an adjudication * * * in and to said stock of the Utah Fuel Company (id.); and

(2) Expressly reserved and retained jurisdiction to fix and allow such compensation (id., Par. 50, R. 77).

The Federal decree was concurred in by these respondents, the Trustees, their counsel, and their bondholders, no objection was taken thereto; it stands unchallenged and unreversed.

Its adjudication binds and estops these respondents from seeking its violation.

And its reservation of jurisdiction precludes any attempt to exercise jurisdiction, whether in accordance or in violation of its terms, by a State court.

The only field of possible dispute that is permitted in these allowance cases by the decisions of this Court in *Brown* v. *Gerdes* (supra) and *Leiman* v. *Guttman* (supra) is whether the Federal Reorganization Court has jurisdiction. Once that premise—here beyond dispute—is found, the conclusion that no state court exercise of jurisdiction is possible, becomes inevitable and inescapable.

The reasons which dictate the rule—enunciated with clarity and cogency in *Brown* v. *Gerdes* and *Leiman* v. *Guttman*—find emphatic documentation here. As provided by Section 77, the reorganized railroad company took the assets of its predecessor company subject to payment of all allowances made by the District Court for reorganiza-

tion services necessarily rendered by parties and counsel. As required by statute, as in all bankruptcy reorganizations, the distributions to creditors were and are to be free of such charges; they are net and are not to be subjected to claims for reorganization services rendered. The consummation decree was here made in terms which expressed and sought to consummate the Congressional intent. The proceeds of the collateral were thus freed so they might be distributed without deduction to these bondholders. The Indenture Trustees and their counsel were fully protected; the consummation decree provided for their compensation as the statute contemplated and required. Yet by this transgression of the express terms of the decree, the $800,000 available to these Refunding and Improvement Mortgage bondholders for their deficiency exceeding $16,000,000, is to be charged with a deduction of $266,427, for allowances of compensation made in denial and violation of the terms of the decree and the underlying statute and without and flaunting the control of the reorganization court. Here, as a result of this state court determination, the control of compensation is not only taken from the Federal Court but the terms of a plan are changed and violated and the distribution to creditors reduced by extramural allowances. The prevention of each of these abuses is an expressed reason for the rule enunciated by this Court in *Brown* v. *Gerdes* and *Leiman* v. *Guttman*. Their presence here demonstrates the need for the rule and its instant application.

The respondents in the courts below have sought to avoid the effect of these controlling decisions of this Court by pointing out that the title to the Utah Fuel stock was not in the old railroad company.

Aside from the fact that the railroad company had a definite interest in the accruals from the Utah Fuel stock (R. 101), which was only cut off by the final plan, the question of title to the Utah Fuel stock is here immaterial,

for it is not to be questioned that the reorganization court took jurisdiction of all collateral held by the bondholders (including the Utah Fuel stock); that, through their Indenture Trustees, the bondholders filed and submitted their claims, liens and collateral to the District Court, and unequivocally submitted themselves to its jurisdiction;* they litigated in the reorganization proceeding the manner of the disposition of the collateral and, specifically, the disposition of the Utah Fuel stock (233 ICC 515, 538, 542, 573); the Trustees sought and received compensation for services rendered in the Reorganization Court and expressly based such claims in part upon services rendered with respect to the disposition of the Utah Fuel stock in the reorganization proceeding and reorganization plans concerning the same and its disposition (242 ICC 629, 640, 641).

But what, of course, is all-important is that the Federal Court expressly adjudicated, in and by the Consummation Decree, that compensation for services to be rendered in the subsequent judicial proceedings affecting the Utah Fuel stock, should be deemed expenses incurred in connection with the "proceedings or the Plan" and should be paid for out of the reorganization funds entrusted to, and by the reorganized railroad company—and the parties concurred in and acted pursuant to the decree up to the final point where they sought to disclaim it by applying to the State Court for allowances.

What is equally of paramount importance is that the Federal Court took and reserved jurisdiction to award these allowances as part of the expense of reorganization and that by reason of rules of res judicata and of estoppel that adjudication cannot be here questioned or challenged (*Chicot County Drainage Dist.* v. *Baxter State Bank*, 308

* The argument of counsel for intervening bondholders that they were not parties bound by the reorganization decree has no weight: their bondholder clients were parties, and the theory of allowance reckons only with reimbursement of the client (*Trustees* v. *Greenough*, 105 U. S. 527).

U. S. 371) and once jurisdiction is found in the Federal Court, that jurisdiction is exclusive under the decisions of this Court.

And what is here of grave public importance is that the rule of exclusive Federal jurisdiction laid down by this Court to implement the protection Congress sought to afford creditors by the revisions of the bankruptcy act against the rapacities of indenture trustees and counsel not selected by them, may not be whittled away by resort to complaisant local Judges or by fine and technical factual distinctions.

Here, when the greater part of the collateral of the bondholders was taken from them by the reorganization court and was no longer available to them upon a foreclosure, *ex* the reorganization, fairness and justice dictated application of the bankruptcy rule that the costs of the foreclosure should be deemed a cost of and should be borne by the general reorganization fund (to which, in the reorganization proceedings, each class of creditor had made its contribution) and not be charged to a minor portion of the collateral, fortuitously or unfortuitously remaining by virtue of the structure of the plan. Fairness and reorganization practice required that the distribution to creditors by way of substitute collateral and the proceeds of sale of the old collateral be net, freed of any part of the reorganization expense. This the Statute and the Federal Court sought to effect under the rule of protection laid down by this Court and it is manifest that justice and equity and the necessity of exercise of the rule are unaffected by any technical argument of where the underlying equity in the Utah Fuel stock lay.

While not daring to deny the jurisdiction of the reorganization court or the plain intendment of the rule adopted by this Court that makes that jurisdiction exclusive, re-

spondents yet managed to argue below that the Consummation Decree left open to the respondents a voluntary choice—an option—to seek compensation elsewhere than through the Federal Court from the reorganized railroad and this despite the express Federal adjudication "that the reorganized company shall pay * * * such amount as may hereafter be approved and allowed by this Court" (Decree, Par. 19, R. 68).

So respondents made the tortuous argument that they may have recourse to the proceeds under the powers granted to them by the Indenture, although they concede, as they must, that the Consummation Decree cancelled the Indentures except insofar as it was necessary to leave the Trustees with power to prosecute the subsequent legal proceedings.

Here, again, we find the injustice of seeking to charge a fraction of the collateral after the major portion of the collateral has been released by the decree of the reorganization court. In making this contention, the Indenture Trustees seem to lose sight of the fact that, at least by modern *mores,* the provisions of an Indenture that permit a Trustee to have compensation for the discharge of his trust duties out of the general funds of the debtor are not designed solely for the benefit of the Trustee; they are inserted primarily for the benefit of the *cestuis.*

These Indentures, as was customary, provided that the primary liability for the expenses of foreclosure should be that of the railroad and that the proceeds of the collateral should be secondarily liable for expenses arising from default. The plan had freed the bulk of the collateral from its secondary liability for expenses incurred by reason of the default; the consummation decree properly freed the remainder and had the railroad assume its primary obligation for both. Nothing else would have been justified, in equity or under bankruptcy practice. The bondholders were entitled to their avails, whether under the statute or under the pledge, free of the cost of reorganiza-

tion or foreclosure. They were entitled to have that expense paid out of the general and available funds of the railroad, both by the terms of the statute and of the pledge. They were entitled to that—as against the railroad—and as against their Trustees. What they were compelled to pay their Trustees under the pledge was a charge for which they were entitled to reimbursement from the railroad. The reorganization decree, in disposing of the underlying liabilities of the railroad, recognized its primary liability under the Indenture for the expenses of foreclosure and properly treated them as part of the expense of reorganization. The Federal Court, in recognition of this, properly adjudged that the railroad should pay these expenses directly, upon application of the Trustees. The Trustees cannot contend, in the face of that adjudication, justified and required by statute and their Indenture, that they may (at their option) violate and transgress this right of their *cestuis*.

CONCLUSION

Wherefore, for the reasons stated, the petition for certiorari should be granted.

Respectfully submitted,

PERCIVAL E. JACKSON,
Counsel for Petitioners.

Dated, June 29, 1951.

APPENDIX

THE PORTION OF THE CONSTITUTION

Article I, Sec. 8(4):

> "*Sec. 8* [*Powers of Congress*] The Congress shall have power * * * (4) To establish * * * uniform Laws on the subject of Bankruptcies throughout the United States."

STATUTES INVOLVED

Sec. 1334 of the 1948 Revised Judicial Code, Title 28, U. S. C.:

> "1334. *Bankruptcy matters and proceedings.* The district courts shall have original jurisdiction, exclusive of the courts of the States, of all matters and proceedings in bankruptcy. (June 25, 1948, c. 646, § 1, 62 Stat. 931.)"

Sec. 77(c)(12) of the Bankruptcy Act, Title 11, U. S. C. § 205:

> "(12) *Compensation for services.* Within such maximum limits as are fixed by the Commission, the judge may make an allowance, to be paid out of the debtor's estate, for the actual and reasonable expenses (including reasonable attorney's fees) incurred in connection with the proceedings and plan by parties in interest and by reorganization managers and committees or other representatives of creditors and stockholders, and within such limits may make an allowance to be paid out of the debtor's estate for the actual and reasonable expenses incurred in connection with the proceedings and plan and reasonable compensation for services in connection therewith by trustees under indentures, depositaries and such assistants as the Commission with the approval of the judge may especially employ."

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ON PETITION FOR A WRIT OF CERTIORARI TO THE APPELLATE DIVISION OF THE SUPREME COURT FOR THE FIRST DEPARTMENT OF THE STATE OF NEW YORK.

BRIEF FOR RESPONDENT THE CHASE NATIONAL BANK OF THE CITY OF NEW YORK, AS TRUSTEE UNDER THE REFUNDING AND IMPROVEMENT MORTGAGE OF THE DENVER AND RIO GRANDE WESTERN RAILROAD COMPANY DATED FEBRUARY 1, 1924, IN OPPOSITION.

ARTHUR A. GAMMELL,
Attorney for Respondent The Chase National Bank of the City of New York, as Trustee.

August 10, 1951.

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Statement.

This Court, in approving the plan for the reorganization under Section 77 of The Denver and Rio Grande Western Railroad Company, in effect decided that, since the Utah Fuel Company stock was accommodation collateral not part of "the debtor's estate", the question of the rights of the

parties in respect of said stock should be decided in "an independent suit in which there is jurisdiction over the proper parties." *R. F. C.* v. *Denver & R. G. W. R. Co.*, 328 U. S. 495, 531 (1946), n. 33.

In the "independent suit", the Supreme Court of the State of New York determined and foreclosed the liens on the Utah Fuel Company stock (R. 135-164), and, among other things, granted allowances to the respondents for services in connection with said suit to be paid out of the proceeds of the foreclosure sale of said stock (R. 12-15).

The petition seeks to review the order of the Appellate Division of the Supreme Court of the First Department of the State of New York (R. 197-199) affirming the order of the Supreme Court of the State of New York (R. 12-15) granting said allowances.

The petitioners believe that the Supreme Court of the State of New York lacked jurisdiction to grant these allowances out of these funds.

The petitioners are holders of bonds for which the respondent The Chase National Bank of the City of New York is trustee.

Said Chase National Bank as trustee believes that the granting of these allowances payable out of said proceeds was in all respects lawful and proper.

Paragraph (12) of subsection (c) of Section 77 (11 U. S. C. § 205(c)(12)) permits the judge to make allowances within limits fixed by the Interstate Commerce Commission "to be paid out of the debtor's estate". The allowances granted in this "independent suit" were not "to be paid out of the debtor's estate".

The language in the order of the reorganization court (R. 68) (the so-called Consummation Decree of the District Court in Colorado) providing for the payment of the compensation and expenses of the three respondents Mortgage trustees and their attorneys in connection with the Utah Fuel Company stock foreclosure action, merely created, it is believed, an alternative source of payment in case proceeds of the Utah Fuel Company stock were not available for the purpose.

In view of the difference of opinion, said Chase National Bank as trustee welcomed the submission of the question to the court.

The Supreme Court of the State of New York decided (R. 185-188) that the granting of these allowances payable out of said proceeds was in all respects lawful and proper; the decision was unanimously affirmed by the Appellate Division (R. 197-199); and a motion for leave to appeal was denied by the Court of Appeals.

This brief is addressed only to the argument that Section 77 or the authorities cited by the petitioners or the so-called Consummation Decree deprives the New York court of jurisdiction to grant the allowances.

ARGUMENT.

Nothing in Section 77 or in the Authorities Cited or in the so-called Consummation Decree Deprives the New York Court of Jurisdiction to Grant the Allowances.

The petitioners rely on *Brown* v. *Gerdes,* 321 U. S. 178 (1944), affirming 290 N. Y. 468, and *Leiman* v. *Guttman,* 336 U. S. 1 (1949), affirming 297 N. Y. 201.

Both these cases dealt with reorganizations under Chapter X of the Bankruptcy Act.

The Denver and Rio Grande Western Railroad Company was reorganized under Section 77 of the Bankruptcy Act.

The provisions of Chapter X as to allowances relate in general to all allowances in respect of services in connection with the reorganization.

Paragraph (4) of Section 221 (11 U. S. C. § 621 (4)) of Chapter X requires the judge as a condition precedent to approving the plan to be satisfied as to

> "* * * all payments made or promised by the debtor or by a corporation issuing securities or acquiring property under the plan *or by any other person,*

> for services and for costs and expenses in, or in connection with, the proceeding or in connection with the plan and incident to the reorganization, * * *." (Emphasis supplied.)

The provisions of Section 77 as to allowances, on the other hand, are in terms limited and relate only to allowances "paid out of the debtor's estate".

Paragraph (12) of subsection (c) of Section 77 (11 U. S. C. § 205(c)(12)) permits the judge to make allowances within limits fixed by the Interstate Commerce Commission "to be paid out of the debtor's estate".

The allowances to which the petitioners object were directed to be paid not "out of the debtor's estate"—but out of the proceeds of accommodation collateral which was no part of the debtor's estate.

The petitioners also rely on *New York Trust Co.* v. *New York & Greenwood Lake Ry. Co.,* 156 F. 2d 701 (C. C. A. 3d, 1946), which dealt with a reorganization of the Erie Railroad Company under Section 77. The decision was in effect that the property covered by the mortgage to the New York Trust Company as trustee was part of the estate of the Erie Railroad Company.

The petitioners further rely on the language in the Decree of the District Court in Colorado (the so-called Consummation Decree).

The Consummation Decree in paragraph 19 (R. 66-68) directs the reorganized Railroad Company to pay the compensation and expenses of the three Mortgage trustees and their attorneys in connection with the "independent suit"—the Utah Fuel Company stock foreclosure action.

But this Decree (R. 58-77) provides that it "neither affects nor purports to affect" the "lien" of any of the three Mortgages, and further provides that

> "* * * with respect to said stock of the Utah Fuel company and the rights and interest therein of the trustees under said mortgages * * *, the aforesaid mortgages are not satisfied, cancelled, and re-

leased by this order but remain in full force and effect." (R. 64-66).

Each of the three Mortgages created a lien on the Utah Fuel Company stock for the payment of the compensation and expenses of the Mortgage trustee and its attorneys. Since the Decree expressly states that it "neither affects nor purports to affect" the liens of any of the three Mortgages and that these liens "remain in full force and effect", the purpose of the Decree could not have been to prevent the enforcement of any of these liens in the "independent suit".

The general language (in paragraph (50)) (R. 77) reserving jurisdiction as to the making of allowances and as to the other matters therein mentioned is no more than the customary language in such decrees expressly keeping alive in case of need jurisdiction as to unfinished matters. Neither this language nor any other language in the Decree is capable of being interpreted as enjoining or prohibiting the enforcement of the liens on the Utah Fuel Company stock for compensation and expenses, or is in any way inconsistent with the express provision quoted above that the liens are not affected but "remain in full force and effect."

Furthermore, the District Court in Colorado had jurisdiction only over the properties of the Railroad Company being reorganized. It had no jurisdiction over the Utah Fuel Company stock. Accordingly, the District Court in Colorado lacked power to exercise jurisdiction to prevent the Court below from enforcing the lien on the Utah Fuel Company stock for allowances according to its terms. As stated by Judge PECORA in the opinion rendered February 16, 1949, determining and foreclosing the liens,

> "The reorganization occurred in the Federal bankruptcy court, and, as is not disputed in this case, concerned only the property of the debtor railroad. That was all that the courts passing on the reorganization had jurisdiction to deal with * * *. Accordingly, the 100,000 shares of the capital stock of the Utah

> Fuel Company, which were not the property of the debtor railroad, were not really involved in that litigation, and their disposition was not even attempted in the reorganization litigation. * * *
>
> "The Utah Fuel Company stock is not the property of the Denver and Rio Grande Western Railroad either as that corporation was before reorganization or as it is now. * * *" *Guaranty Trust Co.* v. *Chase National Bank,* 194 Misc. 628, 630-631 (1949), aff'd 277 App. Div. 767 (1st dept., 1950).

The purpose of the Decree which suggests itself is to prevent any of the three Mortgage trustees or their attorneys from having no source from which to be paid their compensation and reimbursed their expenses in connection with the Utah Fuel Company stock foreclosure action.

The Decree of course required, as a necessary step in the reorganization, the cancellation of the three Mortgages on the railroad properties being reorganized—that is, the properties other than the Utah Fuel Company stock. This cancellation of the liens on the mortgaged properties other than the Utah Fuel Company stock created the possibility of the retained liens on the Utah Fuel Company stock not being sufficient to assure to each trustee a source from which the allowance would be paid. When the Decree was signed no one could tell how the Utah Fuel Company stock foreclosure action would turn out. If, for example, the stock had sold for so small a price that there would have been no excess against which to enforce the lien of the Mortgage under which the Chase National Bank is trustee, neither the trustee nor its attorneys could have been paid except as provided in the Decree. The purpose suggests itself merely to require the payment of the allowances by the reorganized Railroad Company in case the lien turned out to be ineffectual.

CONCLUSION.

The petition should be denied.

Respectfully submitted,

ARTHUR A. GAMMELL,
Attorney for Respondent The Chase National Bank of the City of New York, as Trustee.

August 10, 1951.

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FILED
AUG 7 1961
CHARLES ELMORE CROPLEY
CLERK

IN THE

Supreme Court of the United States

OCTOBER TERM, 1961

No. 179

OPPENHEIMER & HUTZLER, GOLDMAN SACHS & Co., GRAHAM-NEWMAN CORPORATION, NEWMAN & GRAHAM, and ARNHOLD & Co.,

Petitioners,

against

GUARANTY TRUST COMPANY OF NEW YORK, as Trustee under the First Consolidated Mortgage Deed of THE RIO GRANDE WESTERN RAILWAY COMPANY, dated April 1, 1899, JULIUS KLORFEIN, THE CHASE NATIONAL BANK OF THE CITY OF NEW YORK, as Trustee under the Refunding and Improvement Mortgage of The Denver and Rio Grande Western Railroad Company's General Mortgage, dated February 1, 1924, CITY BANK FARMERS TRUST COMPANY, as Trustee under THE DENVER AND RIO GRANDE WESTERN RAILROAD COMPANY'S GENERAL MORTGAGE, dated February 1, 1924, THE DENVER AND RIO GRANDE WESTERN RAILROAD COMPANY, and HAROLD S. BAIRD,

Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE APPELLATE DIVISION OF THE SUPREME COURT FOR THE FIRST DEPARTMENT OF THE STATE OF NEW YORK

BRIEF OF RESPONDENT JULIUS KLORFEIN IN OPPOSITION

BERNARD D. FISCHMAN,
Attorney for Respondent,
Julius Klorfein.

Dated, New York, N. Y., August 7, 1961.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1951

No. 179

OSTERMAN & HUTNER, GOLDMAN SACHS & Co., GRAHAM-NEWMAN CORPORATION, NEWMAN & GRAHAM, and ABRAHAM & Co.,

Petitioners,

against

GUARANTY TRUST COMPANY OF NEW YORK, as Trustee under the First Consolidated Mortgage Deed of THE RIO GRANDE WESTERN RAILWAY COMPANY, dated April 1, 1899, JULIUS KLORFEIN, THE CHASE NATIONAL BANK OF THE CITY OF NEW YORK, as Trustee under the Refunding and Improvement Mortgage of The Denver and Rio Grande Western Railroad Company's General Mortgage, dated February 1, 1924, CITY BANK FARMERS TRUST COMPANY, as Trustee under THE DENVER AND RIO GRANDE WESTERN RAILROAD COMPANY'S GENERAL MORTGAGE, dated February 1, 1924, THE DENVER AND RIO GRANDE WESTERN RAILROAD COMPANY, and HAROLD S. BAIRD,

Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE APPELLATE DIVISION OF THE SUPREME COURT FOR THE FIRST DEPARTMENT OF THE STATE OF NEW YORK

BRIEF OF RESPONDENT JULIUS KLORFEIN IN OPPOSITION

Opinions Below

Leave to appeal was denied without opinion by the New York Court of Appeals (R. 203-204). The Appellate Division, First Department, affirmed without opinion (R. 197-202). The opinion of the New York Supreme Court (R. 185-188) is not reported.

Jurisdiction

Leave to appeal was denied by the Court of Appeals on June 1, 1951 (R. 203-204). The order of the Appellate Division was entered February 27, 1951 (R. 197-202). The jurisdiction of this Court is invoked under 28 U. S. C. § 1257(3).

Question Involved

Whether in a proceeding to foreclose a lien on securities in which the debtor in reorganization had no interest, the state court has jurisdiction to award fees to counsel for services rendered in such proceeding.

Statement of Facts

Pursuant to motion dated August 9, 1950, petitioners sought to intervene "for the purpose of filing objections to allowances made and for rearguing the motions seeking allowances" and, for the purpose of appealing from any allowances which may be granted "out of the fund which was the subject of this action" (R. 18). The opinion of the court authorizing the allowances was filed on August 8, 1950 (R. 179-184), although the formal order was entered on September 14, 1950 (R. 12-15). The New York Supreme Court denied intervention, *inter alia,* for lack of merit (R. 185-188), and the appellate courts unanimously agreed. A summary of the pertinent facts follows:

In 1935, the Denver & Rio Grande Railroad Company filed its petition for reorganization under Section 77 of the

Bankruptcy Act (11 U. S. C. § 205). At that time it had outstanding several classes of bonds, First Consolidated Mortgage bonds (First Consolidated), Refunding & Improvement Mortgage bonds (R & I), and General Mortgage bonds (General)—all secured by various properties of the Denver company. In addition, the First Consolidated also were secured by a first lien upon 100,000 shares of the entire capital stock of the Utah Fuel Company to the extent of $6,000,000, while the R & I had a subordinate lien prior to that of the Generals. The Denver company originally owned the equity of redemption in this stock, but, as a result of a previous reorganization in 1924, one-half of the ultimate beneficial ownership was acquired by the Western Pacific Railroad Corporation and the other by the Missouri Pacific Railroad Company. In consequence, the Denver company relinquished whatever rights it ever had in the Utah Fuel stock.

A plan of reorganization for the Denver company, approved and confirmed by the District Court, was sustained on review by this Court. *R. F. C.* v. *Denver & R. G. W. R. Co.*, 328 U. S. 495 (1945); *Insurance Group* v. *Denver & R. G. W. R. Co.*, 329 U. S. 607 (1947). The plan of reorganization was consummated in 1947 and under its provisions the bondholders received new securities in amounts and proportions not here material. See tables in 328 U. S. at 503. The consummation of the plan released the debtor from any further liability on its outstanding mortgages but expressly left unaffected the respective liens on the Utah Fuel stock. The bankruptcy court did not deal with the Utah Fuel stock, since, as the trial court stated in its 1949 opinion, that stock "is not the property of the Denver & Rio Grande Western Railroad • • • That stock belongs to others", subject to the pledges or liens discussed above, 86 N. Y. S. 2d 505, 508.

Upon consummation of the plans, Guaranty Trust Company, as trustee for the First Consolidated, instituted the proceedings below to foreclose on its prior lien upon the Utah Fuel stock, asserting that the First Consolidated

bondholders had not been paid in full in the bankruptcy reorganization, and that the deficiency was far in excess of $6,000,000, for the collection of which they were entitled to proceed against the collateral pursuant to the terms of the pledge agreement (R. 78-90). As holder of $667,000 principal amount of First Consolidated bonds, Julius Klorfein applied and was allowed to intervene as a party plaintiff (R. 126), and has actively participated in the proceedings through his attorneys, a portion of whose allowance the petitioners are challenging herein. The Chase National Bank, as trustee for the R & I bondholders, filed its answer, conceding the claim of the First Consolidated and claiming only any excess over $6,000,000 which may be realized on the sale or other disposition of the Utah Fuel stock (R. 127). For reasons not here material the Generals opposed the claims of the First Consolidated and of the R & I bondholders.

In the proceedings below, the reorganized Denver company claimed the right to participate in the proceeds of the Utah Fuel stock on a parity with the publicly held First Consolidated and R & I bonds. As noted in the trial court's decision, 194 Misc. 628, 635, 86 N. Y. S. 2d 505, 511, a substantial amount of these securities had previously been pledged as collateral for loans made by the Chase National Bank and by the Reconstruction Finance Corporation (R. 68-71). Sometime after consummation of the plan, the reorganized Denver company paid these loans and the pledged bonds were duly cancelled but stamped with a legend, appearing on all bonds, which left their respective rights in the Utah Fuel stock subject to judicial determination in an independent proceeding. The claim of the reorganized Denver company was predicated upon the following: $1,395,000 face amount of First Consolidated bonds (R. 127-128), as against approximately $15,000,000 in bonds publicly held (R. 84, 148); and about $10,000,000 par amount of R & I bonds, as against $14,000,000 of face amount publicly held (R. 127, 148).

Guaranty Trust Company took no position on the Denver held First Consolidated bonds, while Chase National Bank conceded the validity of the Denver company's claim on the R & I bonds (R. 127). Counsel for respondent Klorfein opposed these claims on the ground that the Denver company, having paid its own debts, may not be subrogated to the rights of its own creditors in the Utah Fuel stock so as to displace or compete with the rights of other creditors who, admittedly, had not been paid in full. This contention was sustained by the trial court (R. 130-131, 142, 425), and affirmed on appeal to the Appellate Division. The Denver company then moved for reargument in order to establish its alleged claim for participation solely upon its holdings of R & I bonds. The motion was opposed by counsel for respondent Klorfein and was denied by the Appellate Division on June 21, 1950. The Denver company did not appeal to the Court of Appeals.

The Utah Fuel stock was sold for $6,800,000. Under the judgment of the court below, this sum, less allowances and expenses, has been substantially distributed among the First Consolidated bondholders in order of their priority, but not including the reorganized Denver company. From the figures cited above, it is readily demonstrable that the elimination of the Denver claim substantially increased the amounts distributable to the public holders of both the First Consolidated as well as the R & I bonds. The public First Consolidated bond holders receive under the judgment of the court below about $500,000 more as a result of the exclusion of the Denver claim, while to the public holders of R & I bonds, even deducting all allowances, the *net* increase to them amounts to about $200,000, since the Denver claim was about 40% of the total R & I claims against the Utah Fuel stock.

For creating or preserving this additional fund for the benefit of both classes of public bondholders, counsel for intervenor Klorfein were allowed a fee of $25,000. As the court below said in its opinion of August 8, 1950 (R. 182):

> "The issue involved the legal question as to whether the bonds in the hands of the defendant railroad were entitled to share in the recovery herein upon a parity with the publicly held bonds. Klorfein's attorneys took charge of that phase of the case, and the court's decision was in favor of the publicly held bonds. The result is that both the First Consolidated and the Refunding Improvement Mortgage bonds are excluded from the recovery herein. The publicly held bonds will therefore receive a larger share of the recovery than they otherwise would have been entitled to receive. Klorfein's attorneys thus obviously rendered a valuable service for which they are entitled to suitable compensation (Nolte v. Hudson Nav. Co., 47 F. 2d, 166, 167)."

In the order settling all allowances, entered on September 14, 1950, the court directed that of this $25,000 allowance,

> "$18,500 shall be charged against the interest of the holders of First Consolidated Bonds in the proceeds of sale, and the balance, $6,797.73 [which includes $297.73 as reimbursement for expenses] shall be charged against the interest of the holders of the Refunding and Improvement Bonds" (R. 14).

ARGUMENT

Petitioners will readily concede that the exclusion of the Denver held R & I bonds substantially increased, as noted above, the amount distributable to the public holders of R & I bonds, and that this addition to their share in the fund was produced by the sole efforts of Klorfein's counsel. It is equally clear from their moving papers and their petition herein that no objection, as such, is raised to the amount awarded to counsel. Their sole contention is that the court below did not have jurisdiction to determine the allowances to counsel; that the bankruptcy court has sole power to award such allowances; and that such allowances are to be paid by the reorganized Denver

company and not out of the fund which counsel for Klorfein had created for the benefit of the R & I bondholders. As for the allowance to counsel for respondent Klorfein, their objection is of course directed only to so much of the order below which directs payment of about $6,900 out of the interests of the R & I bondholders in the fund (R. 14). Obviously, as R & I bondholders, they have no standing to challenge the allowance of $18,500 payable to counsel out of the proceeds to be distributed to the First Consolidated bondholders.

We submit that the petition should be denied because it presents no issue requiring review by this Court. The controversy over the disposition of the Utah Fuel stock was adjudicated in the New York state court because it involved no asset or interest of the debtor within the cognizance of the bankruptcy court. The power of the state court, as a court of equity, to award the fees in question is incidental to the adjudication of that controversy.

1. Under Section 77(a) (11 U. S. C. § 205(a)), exclusive jurisdiction of the bankruptcy court extends to "the debtor and its property", and "as a corollary, over any rights that may be asserted against it," *Callaway* v. *Benton,* 336 U. S. 132, 147 (1949). The bankruptcy court has no jurisdiction to adjudicate rights or controversies in which the debtor has no interest and which do not affect the proper adminstration of the estate. In such situations the parties are remitted to other courts which could more appropriately deal with the issues involved. See *Callaway* v. *Benton,* 336 U. S. 132, 142-143 (1949); *Central Hanover Bank & Trust Co.,* 133 F. 2d 873, 875 (C. A. 2, 1943).

Petitioners do not dispute these elementary principles of bankruptcy reorganization. Nor can it be seriously questioned that at the time when the reorganization proceedings were begun, the Utah Fuel stock was not property of the Denver company. This stock was originally pledged as additional collateral for the various bond issues, and with the transfer of the equity of re-

demption in 1924, this Court noted, the Denver company relinquished whatever right it ever had in the Utah Fuel stock, 328 U. S. at 528. See also *Blair* v. *Coen,* 170 F. 2d 830, 833 (C. A. 7, 1948), certiorari denied, 336 U. S. 954 (1949). The Utah Fuel stock thus became accommodation collateral, which in substance is but a suretyship arrangement to the extent of the pledge. See *Rutherford Nat. Bank* v. *Marriello,* 271 N. Y. Supp. 69, 240 App. Div. 506 (1st Dept. 934), affirmed per curiam 266 N. Y. 568, 195 N. E. 203 (1935). In substance therefore, the suit instituted below as an action for a deficiency claim against a guarantor whose liability to the creditors is, under Section 16 of the Bankruptcy Act (11 U. S. C. § 34), not affected by the discharge of the debtor in bankruptcy. *Union Trust Co.* v. *Willsea,* 275 N. Y. 164, 9 N. E. 2d 820 (1937). Jurisdiction over such a suit accordingly, cannot be asserted in the bankruptcy court. *In re Ninth North Church Street,* 82 F. 2d 186, 188-189 (C. A. 2, 1936); *In re Diversey Bldg. Corp.,* 86 F. 2d 456, 457-458 (C. A. 7, 1936), certiorari denied, 300 U. S. 662 (1936); *Commercial Wholesalers, Inc.* v. *Investors Commercial Corp.,* 172 F. 2d 800, 801 (C. A. 9, 1949).

Jurisdiction over the disposition of the Utah Fuel stock necessarily was vested in the state court below, and as a court of equity having control over the stock, which was no part of the debtor's assets, it has also the incidental inherent power to make allowances chargeable to the fund or against the proportionate share of each class of beneficiaries. "Plainly the foundation for the historic practice of granting reimbursement for the cost of litigation other than the conventional taxable costs is part of the original authority of the chancellor to do equity in a particular situation." *Sprague* v. *Ticonic National Bank,* 307 U. S. 161, 166 (1939); *Woodruff* v. *New York, L. E. & W. R. Co.,* 129 N. Y. 27, 29 N. E. 251 (1891). As the court below stated (555-561):

"The federal courts therefore left to this court the right and duty to foreclose the liens on that stock, and to do whatever else was necessary and incidental to such a foreclosure; to the end that this property (not within the federal jurisdiction) might be effectually and completely dealt with.

* * * * * *

An inevitable part of this power was, therefore, the authority to decide and determine upon the allowances to be made to the parties and their counsel; not only was there authority for such allowance in the mortgages under foreclosure, but also in the inherent power of the court in such an equity action."

* * * * * *

2. Petitioners do not deny that counsel for respondent Klorfein was instrumental in establishing or preserving a fund for the benefit of the R & I bondholders. It follows that the allowances to counsel are properly chargeable to that fund. This is so well established and so widely accepted that a detailed discussion thereof is not necessary. We respectfully invite this Court's attention to *Trustees* v. *Greenough,* 105 U. S. 527, 532-535 (1881); *Sprague* v. *Ticonic National Bank,* 307 U. S. 161, 166-167 (1939); *Nolte* v. *Hudson Nav. Co.,* 47 F. 2d 166, 167 (C. A. 2, 1931); *Farmers Loan & Trust Co.* v. *New York Rys. Co.,* 215 Fed. 712 (C. A. 2, 1914); *Woodruff* v. *New York L. E. & W. R. Co.,* 129 N. Y. 27, 29 N. E. 251 (1891); *Southern Ry Co.* v. *Peck,* 34 N. Y. S. 2d 370 (Sup. Ct. 1942); *New York Cent. R. Co.* v. *New York Harlem R. Co.,* 85 N. Y. S. 2d 112 (Sup. Ct. 1948), and cases there cited. Indeed the benefits thus conferred gives also rise to a lien upon the fund under Section 475 of the Judiciary Law which provides that an attorney has "a lien upon his client's cause of action * * * which attaches to a * * * judgment or final order in his client's favor * * * or the proceeds thereof." See *Fischer-Hansen* v. *Brooklyn Heights R. Co.,* 173 N. Y. 492, 499, 66 N. E. 395, 397 (1903). The absence of a formal retainer is immaterial. *Farmers Loan & Trust Co.* v. *New York Rys. Co.,* 215 Fed. 712 (C. A. 2, 1914).

As beneficiaries of these services, petitioners cannot remit us to another tribunal, which neither has jurisdiction over the controversy nor control over the fund, in order to seek compensation from an adversary party whose right to participate in the fund we have defeated.

Petitioners rely on paragraph 19 of the Consummation Order and Final decree (R. 68). That provision cannot be construed as petitioners suggest. This Court has said that for lack of jurisdiction the plan "did not affect existing rights in the collateral" (328 U. S. at 530, 531) and for the same reason could not undertake to control the matter of fees incident to the disposition of the Utah Fuel stock (R. 64-65). We recognize that in its final decree the bankruptcy court may retain jurisdiction to prevent interference with the execution and operation of the plan, *In re N. Y., N. H. & H. R. Co.*, 160 F. 2d 337, 340 (C. A. 2, 1948), certiorari denied, 329 U. S. 824 (1948); but it cannot do so for the purpose of dealing with matters which are unaffected by the plan and which are beyond the power of the bankruptcy court, *In re Elles Co.*, 174 F. 2d 924, 929 (C. A. 6, 1949); *In re Boston Coal Co.*, 47 F. Supp. 593 (M. D. Pa. 1942). As the trial court said (R. 187):

> "I see nothing in the Colorado decree which compels me to any different result. It cannot, in my opinion, be construed in one breath to renounce jurisdiction over the Utah Fuel stock in favor of this court, and in the next breath, nevertheless, seek to withhold from this court a necessary part of such jurisdiction. Particularly may no such construction be indulged in, since it is clear that the federal court had, and could have, no power over that stock, as it was no part of the property of the debtor."

In any event, to the extent that the consummation order may represent a voluntary undertaking by the reorganized debtor to pay allowances and expenses, it has no relation to the allowance of counsel for respondent Klorfein. The order specifically refers to the indenture trustees only. The controversy raised by the Denver-held

bonds does not even appear to have been contemplated at the time of consummation. The latter controversy first arose after consummation when the reorganized Denver company paid off the loans assumed or extended by the plan. It is hardly likely that the Denver company would consciously assume payment of fees of counsel instrumental in defeating its asserted right to participate in the Utah Fuel stock.

The decisions of this Court in *Leiman* v. *Guttman,* 336 U. S. 1 (1949), and *Brown* v. *Gerdes,* 321 U. S. 178 (1944), do not support petitioners' argument. Theses cases hold that the bankruptcy court has paramount jurisdiction over all fee claims payable by the estate or chargeable against the interests of the estate, or where the fees in question are for services rendered in the bankruptcy proceedings by persons acting in a representative or fiduciary capacity in reorganization. This is an aid of policy of Chapter X of the Bankruptcy Act to secure a fair and equitable reorganization which would be impaired by excessive fees; and under the statute only the bankruptcy court has the judicial responsibility to effectuate that basic policy. No such considerations are applicable to the allowances in question since the subject matter of the controversy is not an interest of the debtor and is beyond the reach of the Bankruptcy Act.

CONCLUSION

The judgment below is correct. There is no conflict with the decisions of this Court. The petition should be denied for lack of merit and for want of a substantial federal question.

Respectfully submitted,

BERNARD D. FISCHMAN,
Attorney for Respondent,
Julius Klorfein.

Dated, New York, N. Y., August 7, 1951.

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IN THE

Supreme Court of the United States

October Term 1951

No. 179

OSTERMAN & HUTNER, GOLDMAN, SACHS & CO., GRAHAM-NEWMAN CORPORATION, NEWMAN & GRAHAM, and ABRAHAM & CO.,

Petitioners,

—against—

GUARANTY TRUST COMPANY OF NEW YORK, as Trustee under the First Consolidated Mortgage Deed of The Rio Grande Western Railway Company, dated April 1, 1899, JULIUS KLORFEIN, THE CHASE NATIONAL BANK OF THE CITY OF NEW YORK, as Trustee under the Refunding and Improvement Mortgage of The Denver and Rio Grande Western Railroad Company, dated February 1, 1924, CITY BANK FARMERS TRUST COMPANY, as Trustee under The Denver and Rio Grande Western Railroad Company's General Mortgage, dated February 1, 1924, THE DENVER AND RIO GRANDE WESTERN RAILROAD COMPANY, and HAROLD S. BAIRD,

Respondents.

BRIEF OF RESPONDENT GUARANTY TRUST COMPANY OF NEW YORK, AS TRUSTEE UNDER THE FIRST CONSOLIDATED MORTGAGE DEED OF THE RIO GRANDE WESTERN RAILWAY COMPANY DATED APRIL 1, 1899, IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

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Guaranty Trust Company
of New York, Trustee
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In the

Supreme Court of the United States

October Term 1951

No. 179

Osterman & Hutner, Goldman, Sachs & Co., Graham-Newman Corporation, Newman & Graham, and Abraham & Co.,

Petitioners,

—against—

Guaranty Trust Company of New York, as Trustee under the First Consolidated Mortgage Deed of The Rio Grande Western Railway Company, dated April 1, 1899, Julius Klorfein, The Chase National Bank of the City of New York, as Trustee under the Refunding and Improvement Mortgage of The Denver and Rio Grande Western Railroad Company, dated February 1, 1924, City Bank Farmers Trust Company, as Trustee under The Denver and Rio Grande Western Railroad Company's General Mortgage, dated February 1, 1924, The Denver and Rio Grande Western Railroad Company, and Harold S. Baird,

Respondents.

BRIEF OF RESPONDENT GUARANTY TRUST COMPANY OF NEW YORK, AS TRUSTEE UNDER THE FIRST CONSOLIDATED MORTGAGE DEED OF THE RIO GRANDE WESTERN RAILWAY COMPANY DATED APRIL 1, 1899, IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

Decisions and Opinions Below

There were two opinions handed down by the Trial Court. On September 14, 1950 the Trial Court handed down an opinion in connection with the making of an

order granting allowances (R. 179), and then on October 5, 1950, it wrote a second opinion (R. 185). The occasion for the second opinion was the denial of a motion made by the present petitioners for leave to intervene in the action (R. 18 *et seq.*). That motion was based solely on petitioners' theory that the state court lacked jurisdiction to grant allowances payable out of the proceeds of sale; it did not question the reasonableness of the amounts allowed. The second opinion dealt both with petitioners' alleged right to intervene and also at some length with the question of the state court's jurisdiction to grant allowances.

The order granting allowances was unanimously affirmed without opinion by the New York Appellate Division, First Department (R. 197-199). A motion for leave to appeal was denied by the Court of Appeals (R. 203-204).

The order denying petitioners' motion for leave to intervene was likewise unanimously affirmed by the Appellate Division with a modification which related only to the hearing of that appeal (R. 200-202).

Statement as to Jurisdiction

Petitioners claim that the order granting allowances which they now seek to have reviewed violates their rights under the Bankruptcy Act and also under that section of the Constitution which empowers the Congress to establish uniform laws on the subject of bankruptcies (Petition, pp. 2-3, and Appendix thereto).

In behalf of respondent, Guaranty Trust Company of New York, as trustee (hereinafter called Guaranty), it is suggested that there is no jurisdiction because:

1. The Bankruptcy Act is not involved and therefore no Federal question is presented.

2. Petitioners never became parties to the action and accordingly have no standing in this Court.

Statement of the Case

The action was brought by Guaranty to foreclose a collateral pledge of the capital stock of Utah Fuel Company. The pledge had been made in 1901 by the then owners, Spencer Trask & Co., as accommodation collateral security for the payment of the principal and interest of the bonds (hereinafter called Consols), secured by the First Consolidated Mortgage Deed of The Rio Grande Western Railway Company. The extent of the pledge was $6,000,000. Possession of the certificates passed to Guaranty.

Subsequently, and in connection with a reorganization of the successor railway, The Denver Rio Grande and Western (hereinafter called Denver), subordinate liens on the same stock were created first in favor of the Refunding and Improvement Bonds (hereinafter called Refundings), represented by The Chase National Bank of the City of New York (hereinafter called Chase), as trustee, and lastly in favor of the General Mortgage Bonds, represented by the City Bank Farmers Trust Company (hereinafter called City Bank), as trustee. The equity of redemption was transferred in due course to Western Pacific Railroad Corporation and Missouri Pacific Railroad Company.

The records of this Court show that the Denver was reorganized under the Bankruptcy Act, and that on two occasions this Court considered and approved the Denver Plan. *R. F. C.* v. *Denver &c. Ry.*, 328 U. S. 495 (hereinafter referred to as the first Denver case) and *Insurance Group* v. *Denver &c. Ry.*, 329 U. S. 607 (hereinafter referred to as the second Denver case).

As the equity of redemption in the Utah Fuel stock did not belong to the Denver, the Bankruptcy Court had no jurisdiction over it, and accordingly Guaranty began the present action in the New York State court which did have

jurisdiction. Under the final judgment, the stock was sold at foreclosure and brought $6,800,000.

Petitioners do not attack the jurisdiction of the state court in the foreclosure proceedings, or the propriety of its final judgment of foreclosure and sale of the Utah Fuel stock. They assert merely that while the state court had full jurisdiction over the foreclosure and sale, it nevertheless had no jurisdiction whatever to make any allowances to the Trustees or their counsel or to any of the other parties in the foreclosure proceedings, and that in respect to all such allowances the parties should have made application to the Bankruptcy Court in Denver, which had nothing to do with the foreclosure action and which never had any jurisdiction over the subject matter of that action.

POINT I

The Bankruptcy Act is not involved and therefore no Federal question is presented.

This action is not ancillary to the Denver reorganization, but is a wholly independent plenary action brought in a New York state court by a New York pledgee to foreclose a lien created by a New York contract on property which formed no part of the bankrupt estate. It is therefore misleading to say (petition p. 4) that parties to the reorganization proceedings instituted the action. It was instituted, as the complaint shows (R. 78), by the Guaranty as pledgee in the state court because of the want of jurisdiction in the Bankruptcy Court. Of course, if the Bankruptcy Court had had jurisdiction of the stock it would have disposed of it in the reorganization. That would have been its duty.

As, however, the New York court alone had jurisdiction of the stock, necessarily it alone had jurisdiction of

the proceeds which replaced the stock after the foreclosure sale. The Bankruptcy Court which for lack of jurisdiction could not deal with the stock, could not assume or acquire jurisdiction of the proceeds after they had come into the hands of the New York court.

The matter was carefully analyzed in the second opinion of Mr. Justice Pecora (R. 185-188). With reference to the jurisdiction of the state court, he says:

> "The fundamental consideration which the moving parties overlook is the fact that this court is dealing with an action and property over which the federal courts never had any jurisdiction. The reorganization proceedings were concerned only with the property of the debtor railroad; and concededly the Utah Fuel Company stock never was any part of the debtor's estate. If it had been, it would have been disposed of in the reorganization proceedings. As that stock was not any part of the property of the debtor, the federal courts have heretofore recognized that they had no jurisdiction to foreclose the liens thereon and to make disposition thereof. The federal courts therefore left to this court the right and duty to foreclose the liens on that stock, and to do whatever else was necessary and incidental to such a foreclosure; to the end that this property (not within the federal jurisdiction) might be effectually and completely dealt with. Thus because the federal reorganization court clearly had no jurisdiction, and this court on the contrary clearly did have jurisdiction, a suit was duly instituted in this court in order to secure a full and complete adjudication of the rights of all the parties thereto.
>
> "Now what had to be done to accomplish such an adjudication? Of course the liens had to be adjudged and defined; their true amounts had to be ascertained,

and the deficiencies thereunder had to be duly fixed; a sale of the pledged stock had to be made; the costs and expenses had to be paid, and distribution of the remaining proceeds had to be effected. No lesser exertion of power would obviously be consonant with common sense, with due justice to the parties, and with a proper regard for the right and duty of the court in the exercise of its conceded jurisdiction over the res in question and the parties before it.

"An inevitable part of this power was, therefore, the authority to decide and determine upon the allowances to be made to the parties and their counsel; not only was there authority for such allowance in the mortgages under foreclosure, but also in the inherent power of the court in such an equity action. 'Plainly the foundation for the historic practice of granting reimbursement for the cost of litigation other than the conventional taxable costs is part of the original authority of the chancellor to do equity in a particular situation' (Sprague v. Ticonic Bank, 307 U. S., 161, 166).

"Equally clearly those costs and allowances had to be fixed before anything could be paid over to the bondholders entitled to receive the remaining proceeds. Hence it is manifest that the jurisdiction in this case extended, and had to extend, to the making of the allowances in question. It could not well be otherwise. Not only was this court the best advised of any tribunal concerning what should be allowed; but if, as asserted by the moving parties, the matter of such allowances lay wholly and exclusively within the power of the Colorado federal court, then it is clear that no genuinely final determination could be made in this action until after such federal court had fixed those

allowances. And what would happen if, as is conceivable, the federal court saw fit never to take such action, or saw fit inordinately to delay it? The courts of this state would, in such event, be powerless to remedy such a situation; and this cause might then eventuate in an utter futility, or justice therein be indefinitely and helplessly postponed. Such a consequence only makes more evident the clear necessity for the possession by this court of plenary jurisdiction over the res and the parties in this action; and such jurisdiction, I am convinced that it has, should have, and must exercise.

"I see nothing in the Colorado decree which compels me to any different result. It cannot, in my opinion, be construed in one breath to renounce jurisdiction over the Utah Fuel stock in favor of this court, and in the next breath, nevertheless, seek to withhold from this court a necessary part of such jurisdiction. Particularly may no such construction be indulged in, since it is clear that the federal court had, and could have, no power over that stock, as it was no part of the property of the debtor."

To read the Consummation Order (R. 58), as petitioners do, as an attempt by the District Court to control the New York court in the conduct of foreclosing a lien on property not belonging to the Debtor is obviously to misread the order. The jurisdiction of the District Court was exclusive as far as it went, but it was limited to the Debtor and its property. The very cases cited by petitioners rest on this principle.

Leiman v. *Guttman,* 297 N. Y. 201, affirmed 336 U. S. 1, was an action in the State court on a contract which provided for counsel fees. The services for which the action was brought had been rendered in reorganization proceed-

ings brought under the Bankruptcy Act in the Federal courts. The facts are almost the reverse of ours. There the proceeding in which the services were rendered was a bankruptcy matter, here it was not; there the services were rendered in a Federal court, here they were not; there the Federal Judge was personally familiar with the nature and extent of the services, here it was the State Judge who had these advantages.

Matter of Brown (*Gerdes*), 290 N. Y. 468, affirmed *sub nom. Brown* v. *Gerdes,* 321 U. S. 178, concerned services rendered in an action in a state court by counsel representing the bankrupt estate. Any allowances that were made would have to be paid by the bankrupt estate. For that reason it was held that the Federal court had exclusive jurisdiction.

On page 181 of the opinion this Court says:

> "Sec. 77B, like §77 of the Bankruptcy Act, had as one of its purposes the establishment of more effective control over reorganization fees and expenses * * * in recognition of the effect which a depletion of the cash resources of the estate may have on both the fairness and feasibility of the plan of reorganization."

In that sentence, we submit, is to be found the real basis for exclusive Federal jurisdiction of fees for services rendered in state courts, where such exclusive Federal jurisdiction exists. If the Debtor were asked to pay, the Federal court alone could fix allowances. The principle involved, however, has no bearing on fees earned in a state court foreclosure action which were payable from a source which was wholly outside the Debtor's estate, and of which the state court had exclusive jurisdiction.

Nor is it correct to argue that payment of expenses and compensation out of the proceeds in any way infringes on

the Plan, for, as the stock did not belong to the Debtor, the Plan (254 ICC 349, 398-399) could not and did not purport to award it to bondholders; the Plan recognized that the plaintiff, as trustee, had a lien on it which was not enforceable in the Federal court.

The Plan gave bondholders only new railroad securities. It then left the stock, over which the Bankruptcy Court never had any jurisdiction, in the possession of the trustee which had it, to be distributed by that trustee under the power given by the mortgage or foreclosed in a court which had the necessary jurisdiction.

The District Court could not "reserve", a jurisdiction it never had; of course it did not purport to. It had jurisdiction over the Debtor. It alone could have required the Debtor to pay, but it did not rule that a state court having exclusive jurisdiction over stock that did not belong to the Debtor was not free to foreclose a lien on it, or to pay proper expenses and allowances out of the proceeds of sale.

The intention of the District Court clearly appears from the fact that in the Consummation Order (R. 58) it provided that (R. 63-64) the First Consolidated Mortgage, the Refunding and Improvement Mortgage and the General Mortgage should be satisfied, cancelled, and released, "provided, however, that this order neither affects nor purports to affect:

> "(A) The lien of the above-mentioned First Consolidated Mortgage of The Rio Grande Western Railway Company on the 100,000 shares of capital stock of the Utah Fuel Company, heretofore deposited and pledged with the trustee under said mortgage under a Pledge Agreement dated May 23, 1901, or the rights of the trustee as pledgee thereof" (R. 64).

Similar provisions are made (R. 65) with reference to the continuing liens of the Refunding and of the General mortgages on the same stock.

The lien of the First Consolidated Mortgage, so reserved expressly included a lien for services (R. 124).

The lien of the mortgage is applicable not only to the railroad securities pledged thereunder, but also to the collateral. This is established by the pledge agreement, which provides (R. 94):

> "The said stock shall be held by the said Morton Trust Company [corporate predecessor of Guaranty] as such Trustee as security for the payment of the principal and interest of the bonds of the said Rio Grande Western Railway Company secured by said first consolidated mortgage and in all respects subject to the terms and conditions of said mortgage with reference to the railroad securities pledged thereunder * * *"

In other words, the stock was pledged subject to all the provisions of the mortgage (R. 94); the mortgage contained a provision giving the trustee a lien on pledged securities for the costs and expenses of the sale including reasonable compensation to the trustee and to its agents, attorneys, and counsel (R. 92); and this provision of the mortgage was by the Consummation Order expressly preserved (R. 64) although in all other respects the mortgage was declared null and void, satisfied, cancelled, and released (R. 64).

POINT II

Petitioners never became parties to the action and accordingly have no standing in this Court.

In this action, Chase as trustee represented all the holders of the Refundings, including the petitioners. Petitioners were content with this representation until August 9, 1950 when they moved to intervene in the action (R. 18-19). The controlling New York statute is Section 193-b of the Civil Practice Act. By that statute, intervention can be had only "upon timely application". Petitioners' motion was not made until after the question which they sought to raise had been adjudicated.

The final judgment, made September 23, 1949 (R. 135) contained a provision (R. 161) which determined the right to have allowances paid out of the proceeds of sale. Before petitioners moved, this judgment had been unanimously affirmed by the Appellate Division (277 App. Div. 767). Subsequently it was also affirmed by the Court of Appeals (302 N. Y. 658). Under New York law, as determined by the New York court in this case (R. 185, at 188) petitioners' application was not timely.

As it happened, however, petitioners waited until the situation had been even further crystallized before they attempted to intervene. In due course various parties moved for allowances. It was not until after these motions were granted, and specific amounts had been awarded to parties and counsel, and the decision had been printed in the New York Law Journal, that petitioners moved. Their motion papers contain the statement (R. 29):

> "The opinion of Mr. Justice Pecora on the application for allowances appears in the New York Law Journal of this date and is incorporated by reference herein."

It is therefore inaccurate to say (petition p. 6):

> "The state court judge, over the objection of these petitioners, made an order granting to respondent-trustees and their counsel and to counsel for respondent bondholder-intervenors allowances aggregating $266,427 * * *."

October 5, 1950 their motion to intervene was denied (R. 15-17).

February 27, 1951, the order was unanimously affirmed by the Appellate Division (R. 200-202) without opinion, and with a modification (R. 202) which, an inspection shows, related only to the hearing before the Appellate Division.

Petitioners have failed to include in the Record prepared by them the papers showing that on April 4, 1951, they moved in the Appellate Division for leave to appeal to the Court of Appeals from the affirmance of the order denying their motion to intervene and that the Appellate Division, without opinion, denied their motion.

Who can intervene in a New York case under the New York statute and in what circumstances are clearly questions for New York courts. In the present instance, the Trial Court and the Appellate Division have both held that these petitioners may not intervene. Their motion was denied (R. 15). Yet the petition (p. 1) casually refers to the petitioners as "intervenors below".

The force of the New York decisions is not lessened because the Trial Court and the Appellate Division graciously listened to petitioners on the merits, and pointed out that on the merits, too, under New York law, petitioners must fail.

CONCLUSION

The petition should be denied.

Dated, New York, August 1, 1951.

Respectfully submitted,

THEODORE KIENDL
Attorney for Respondent
Guaranty Trust Company
of New York, as Trustee.

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IN THE

Supreme Court of the United States

OCTOBER TERM 1951.

No. 179.

OSTERMAN & HUTNER, GOLDMAN, SACHS & CO., GRAHAM-NEWMAN CORPORATION, NEWMAN & GRAHAM, and ABRAHAM & CO.,

Petitioners,

—against—

GUARANTY TRUST COMPANY OF NEW YORK, as Trustee under the First Consolidated Mortgage Deed of The Rio Grande Western Railway Company, dated April 1, 1899, JULIUS KLORFEIN, THE CHASE NATIONAL BANK OF THE CITY OF NEW YORK, as Trustee under the Refunding and Improvement Mortgage of The Denver and Rio Grande Western Railroad Company, dated February 1, 1924, CITY BANK FARMERS TRUST COMPANY, as Trustee under The Denver and Rio Grande Western Railroad Company's General Mortgage, dated February 1, 1924, THE DENVER AND RIO GRANDE WESTERN RAILROAD COMPANY, and HAROLD S. BAIRD,

Respondents.

BRIEF ON BEHALF OF RESPONDENT, CITY BANK FARMERS TRUST COMPANY, AS TRUSTEE, UNDER THE GENERAL MORTGAGE DATED FEBRUARY 1, 1924, MADE BY THE DENVER AND RIO GRANDE WESTERN RAILROAD COMPANY.

Opinions Below.

[Figures in parentheses refer to folios of Record in the New York courts.]

Although the petition refers to only one opinion below—that at page 179 of the Record (535-552), there was another opinion of the Supreme Court of the State of New York (New York County), the

second (553-564) being that of September 14, 1950. On the latter was based the order denying intervention to the petitioners, Osterman & Hutner, *et al.* Neither opinion was officially reported.

On February 27, 1951, both orders were affirmed by the Appellate Division, First Department, the second with slight modification. See 278 App. Div. 650, memorandum opinions Nos. 3 and 4.

On April 24, 1951, the motion of these petitioners for leave to appeal to the Court of Appeals was denied by the Appellate Division at 278 App. Div. 765. Leave to appeal also was denied by the Court of Appeals on June 1, 1951, without opinion, memorandum decision not yet reported.

Questions Presented.

The first question presented is whether these petitioners have any standing to file a petition for writ of certiorari.

A second question is whether any principle of federal law deprives the New York courts of jurisdiction to grant allowances for services performed in independent litigation in the New York courts to be paid out of the fund being administered by the New York courts.

A third question is whether this Court should review a state court decision resting upon a non-federal ground which independently and adequately supports the state court judgment.

Statement.

The New York action was commenced in 1947 by the trustee under the Rio Grande Western Railway Company First Consolidated Mortgage to foreclose a lien on 100,000 shares of Utah Fuel Company stock pledged thereunder in 1901. This respondent, City Bank Farmers Trust Company, as trustee under The Denver and Rio Grande Western Railroad Company (herein called the "D&RGW") General Mortgage, admittedly a holder of a lien on the Utah Fuel stock, was named a defendant, together with other parties.

On March 4, 1949 the Supreme Court of the State of New York entered an interlocutory judgment (373-401) and on September 23, 1949 the same court entered a final decree (403-533). By paragraph (3) of such final decree the New York court held, in part, as follows:

> "(3) That this Court hereby reserves jurisdiction to make such allowances as may be just and lawful for the payment of * * * the fees or other compensation and expenses of * * * any party to this action who may by law be entitled thereto, out of the proceeds of sale. After payment of said fees, compensation and expenses, the remainder of the proceeds of said sale shall be distributed as follows: * * *" (483).

By paragraph (5) of said final decree it held as follows:

> "(5) That this Court hereby reserves jurisdiction to determine all questions relating to costs, compensation, allowances, disbursements and ex-

penses in connection with this action and the sale to be made pursuant to this Final Judgment and Decree and all questions relating to the enforcement of this Final Judgment and Decree." (491-2)

No party to the action objected to either of the above-quoted provisions of the final decree. Appeals were taken on other grounds, but the final decree was affirmed by the Appellate Division, First Department, on May 23, 1950, 277 App. Div. 767, 97 N. Y. S. 2d 542; and by the Court of Appeals on March 8, 1951, 302 N. Y. 658, 98 N. E. 2d 474.

In the meantime, on April 11, 1950, pursuant to said interlocutory judgment, the Utah Fuel stock was sold at public auction for $6,800,000.

On June 28, 1950 the petitioners, Osterman & Hutner, a brokerage firm, wrote to Justice Pecora (88) of the Supreme Court of the State of New York (New York County), making the contention that any allowances for services in the New York litigation should be made by the federal reorganization court and paid by the reorganized D&RGW.

On June 30, 1950 Justice Pecora's secretary replied to this brokerage firm, stating that it was the court's feeling that Osterman & Hutner's position should be presented through counsel (80).

On July 5, 1950 the brokerage firm again wrote to the New York court stating it was delaying until after July 27, 1950 any application for intervention (81).

On August 7, 1950 Osterman & Hutner employed counsel who communicated with the New York court and "found that Judge Pecora had already prepared his decision" (82).

On August 8, 1950 Justice Pecora filed his opinion granting allowances to certain parties and their counsel for services in the New York litigation (535, 552).

On or after August 9, 1950 these petitioners filed a notice of motion in the New York courts for leave to intervene. That motion was denied by the New York court (553-564; 44-51). Subsequently the Appellate Division modified the order "to the extent of granting the application to intervene, *for the purpose of this appeal* * * *" (278 App. Div. 650; emphasis supplied).

The petitioners base their objections to the New York court's action upon provisions of a Consummation Order entered in a federal reorganization case in which the D&RGW was reorganized. Here also a brief chronological outline is of interest:

October 24, 1943—The District Court entered its Approval Order, approving the plan of reorganization (herein called the "Plan") of the D&RGW and held it to be fair and equitable.

November 1, 1944—The District Court entered its Confirmation Order, which confirmed the Plan, following the vote of creditors, and repeated the holding that the Plan was fair and equitable.

June 10, 1946—This Court affirmed the Approval Order and the Confirmation Order, in *R. F. C.* v.

Denver & RGWR Co., 328 U. S. 495. The Plan was that previously formulated by the Interstate Commerce Commission, so approved and confirmed, as interpreted by this Court's June 10, 1946 opinion.

April 10, 1947—The District Court's Consummation Order was entered.

ARGUMENT.

I.

The petitioners have no standing to file the petition.

The order of the Appellate Division, unanimously affirming the lower court's order denying the petitioners' application for leave to intervene, modified that order to the extent only of allowing intervention for the purpose of "this appeal"—*i. e.,* the appeal to the Appellate Division from the order granting allowances. The Appellate Division said, however:

> "* * * we think Special Term was justified, in the exercise of discretion, in denying the application of Osterman & Hutner, *et al.* for leave to intervene as parties to the action." (278 App. Div. 650)

That limited purpose (of intervention for the purpose of having the appeal considered by the Appellate Division) was fully availed of. Intervention was denied for all other purposes. The Court of Appeals refused to consider an appeal by the petitioners.

The attempted intervention was not timely, whether considered in relation to the final judgment of September 23, 1949 or the decision of August 8, 1950, granting allowances, and the order entered thereon on September 14, 1950.

Of course, even if these petitioners had been permitted to intervene, they would have entered the litigation subject to all action therein prior to their application to intervene. This means that they would have entered subject to the determination made in the final decree of September 23, 1949 whereby the court provided for the making of allowances for "compensation and expenses * * * of any party to this action who may by law be entitled thereto, out of the proceeds of sale" (483).

Nor can it be claimed by the petitioners that the decree provision that compensation would be awarded to parties "by law entitled thereto" was not interpreted by them as meaning that allowances would be made to the parties enumerated in the September 14, 1950 allowance order. First, the fact that petitioners may have incorrectly construed the 1949 final decree does not change its legal significance or the consequences flowing from it. In addition, the petitioners were entirely familiar with the construction being placed on the final decree by the other parties and they had been advised by the court that, if they wished to present their views to the court, they should do so through counsel.

When these petitioners at last did make application to intervene, the decision of the New York court had already been announced. First, they relied on a backdoor attempt to forestall the granting of allowances

out of the fund in court. Then, after a decision adverse to their contention, they attempted to intervene and have the question re-litigated. Justice Pecora in his decision denying leave to intervene stated (563-4):

> "Hence, if these movants are not indeed barred by the rule of *res adjudicata,* they are by their *laches.*"

II.

The petitioners have failed to show that a federal question is presented or any grounds for disregarding in this case the general and proper principle of equitable procedure, that a fund should bear the expenses of its own administration.

The established principle of equitable procedure that a fund should bear the expenses of its own administration has been developed over the years in cases well known to this Court. See *Trustees* v. *Greenough* (1881), 105 U. S. 527; *Sprague* v. *Ticonic Bank* (1939), 307 U. S. 161. The petitioners apparently do not question such general equity power but ask this Court to review its exercise by the New York courts on the ground that the reorganization court had exclusive jurisdiction to determine allowances in the New York litigation.

The petitioners suggest that something in the Consummation Order entered in the reorganization case on April 10, 1947 had the effect of embodying in the Plan new provisions limiting the rights of the three mortgage trustees in connection with any independent suit that might be filed to foreclose on the Utah Fuel stock. Furthermore, they assert that the Consum-

mation Order provisions had the effect of altering the Plan, and of holding that the Plan, with such new provisions included, would be fair and equitable—but that, without these new provisions, the Plan would not be fair and equitable. Obviously the Consummation Order, a procedural order, entered almost one year after this Court had approved, confirmed and interpreted the Plan, could not change the Plan.

It is clear from an examination of the Consummation Order (186-8, 197-202) that the purpose of the provisions relied upon by the petitioners was solely to give the three mortgage trustees an equitable substitute for the protection previously furnished them by their respective liens on the D&RGW assets. Even this respondent, the most junior General Mortgage trustee, had had a lien—prior to that of the General Mortgage bonds—upon assets which were sufficiently valuable to warrant the issuance of $4,354,816 par value of new common stock, which the New York court found to have an "actual value" as of the date of distribution of $430,038 (441). After the Plan was consummated, the mortgage trustees would no longer be able to rely upon their respective liens on the railroad property for their compensation and expenses. It was always possible that a court taking jurisdiction of the litigation to be brought for foreclosure on the Utah Fuel stock might take the view (as was in fact urged by at least one of the parties to the New York case) that unsuccessful litigants, even though indenture trustees and necessary parties, should not receive compensation out of the proceeds of sale of the Utah Fuel stock.

The two decisions of this Court (*Brown* v. *Gerdes*, 321 U. S. 178, and *Leiman* v. *Guttmann*, 336 U. S. 1),

relied upon by petitioners as establishing exclusive jurisdiction in the reorganization court to fix and pay the compensation of parties to the state court action, are not in point. Both decisions relate to services rendered in a federal reorganization proceeding. In the first case, attorneys had been appointed by the bankruptcy court to bring suit in a state court upon causes of action constituting assets of the bankruptcy estate. In the second case, a stockholders' committee had entered into a private agreement with its attorneys to pay them compensation for services in the reorganization proceeding in addition to the fees allowed out of the general estate of the debtor. It is clear that the facts in the present case are entirely dissimilar.

Here the reorganization court, in entirely separate litigation, in which the court did not have jurisdiction of the *res* (the Utah Fuel stock) nor of at least one of the necessary parties (Alexander, as trustee), obviously would not and could not rob the New York courts of jurisdiction that under fundamental equity principles is theirs. This jurisdiction (of the *res* and of the parties) was as completely independent of the reorganization proceeding as if that reorganization proceeding had never occurred. The New York courts had exclusive jurisdiction to determine the rights in the stock, to direct its sale and to order the disposition of its proceeds. No federal question is presented.

III.

This Court has established a rule that it will not review a state court decision resting upon a non-federal ground which independently and adequately supports the state court.

This rule was stated by Mr. Justice Sutherland in *Fox Film Corporation* v. *Muller* (1935), 295 U. S. 207, at p. 210, where he held:

> "* * * the case is controlled by the settled rule that where the judgment of a state court rests upon two grounds, one of which is federal and the other non-federal in character, our jurisdiction fails if the non-federal ground is independent of the federal ground and adequate to support the judgment."

Also see the cases there cited and *Herb* v. *Pitcairn* (1944), 324 U. S. 117, 125.

The New York court decision refusing intervention to these petitioners was based, *inter alia,* upon the principles of *res judicata* and *laches* (563-4). Both of these grounds, independently and adequately, support the state court judgment. Neither of these grounds involves a federal question. Thus, whether or not other grounds here urged by the petitioners have merit (and this respondent submits they do not), the action of the New York courts may be fully sustained under the doctrine either of *res judicata* or of *laches,* as applied by the New York courts.

Conclusion.

The petitioners, Osterman & Hutner, *et al.*, have no standing to file a petition for writ of certiorari herein. Moreover, assuming that this were not so, the petition should be denied because (a) it fails to state a federal question, and (b) the decision of the New York courts is, in any event, independently and adequately supported by non-federal grounds for such decision.

Respectfully submitted,

JOHN B. MARSH,
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Attorneys for Respondent City Bank Farmers Trust Company, as Trustee.

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Of Counsel.

July 31, 1951.

AUG 21 1951
CHARLES ELMORE CROPLEY
CLERK

Supreme Court of the United States

OCTOBER TERM 1951

No. 179

OSTERMAN & HUTNER, GOLDMAN SACHS & Co., GRAHAM-NEWMAN CORPORATION, NEWMAN & GRAHAM, and ABRAHAM & Co.,

Petitioners,

against

GUARANTY TRUST COMPANY OF NEW YORK, as Trustee under the First Consolidated Mortgage Deed of THE RIO GRANDE WESTERN RAILWAY COMPANY, dated April 1, 1899, JULIUS KLORFEIN, THE CHASE NATIONAL BANK OF THE CITY OF NEW YORK, as Trustee under the Refunding and Improvement Mortgage of The Denver and Rio Grande Western Railroad Company's General Mortgage, dated February 1, 1924, CITY BANK FARMERS TRUST COMPANY, as Trustee under THE DENVER AND RIO GRANDE WESTERN RAILROAD COMPANY'S GENERAL MORTGAGE, dated February 1, 1924, THE DENVER AND RIO GRANDE WESTERN RAILROAD COMPANY, and HAROLD S. BAIRD,

Respondents.

REPLY BRIEF OF PETITIONERS IN SUPPORT OF APPLICATION FOR WRIT OF CERTIORARI

PERCIVAL E. JACKSON,
Counsel for Petitioners.

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Respondents' briefs clearly reveal that there is no adequate answer on the merits to this petition and, in lieu thereof, their principal attempt is to avoid such consideration, by appeal to technicalities.

I

Certain of the respondents, Guaranty Trust Company and City Bank Farmers Trust Company, would seek to avoid consideration of the petition on its merits, by the contention that petitioners do not have standing to file the petition for the reason that they were not granted the status of parties below.

That contention is patently without merit. The Appellate Division of the Supreme Court expressly granted petitioners intervention in the proceeding for appeal purposes (R. 202).

In any event, petitioners, as holders of bonds adversely affected by the adjudication below, have status to appeal (*Cohen* v. *Young*, 127 F. 2d 721, 724; *Hobart* v. *Hobart*, 86 N. Y. 636; *Gats* v. *Gats*, 275 App. Div. 771, 87 N. Y. S. 2d 621; 6 Carmody on N. Y. Pleading and Practice, Section 63).

These respondents made the same contention before the Court of Appeals, on petitioners' motion for leave to appeal to that Court. Respondents urged there, too, and on like grounds that petitioners were not parties and therefore did not have status to move for leave to appeal. Respondent, Guaranty, urged, on that basis, that the motion be dismissed. And had petitioners no right to seek leave, their motion would have been dismissed, under the practice of that Court (*Morris* v. *Chemical Bank & Trust Company*, 291 N. Y. 646, 51 N. E. 2d 930; *In re John Case, et al.*, 292 N. Y. 575, 54 N. E. 2d 691; *People* v. *Whitcomb*, 298 N. Y. 635, 82 N. E. 2d 30). The refusal of the Court of Appeals to dismiss (R. 204) conclusively establishes the right of these petitioners to seek appellate review.

II

Respondent, City Bank, contends that the Federal questions posed by petitioners are not reached for the reason

that the provision of the final judgment (R. 161) in which the Court reserved jurisdiction "to make such allowances as may be just and lawful for the payment of the expenses * * * of any party to this action who may by law be entitled thereto, out of the proceeds of sale * * *," warranted the granting of the allowances challenged on grounds of res judicata.

It should be unnecessary to labor the proposition that a judgment that provides for such allowances as may be just and lawful to parties who may by law be entitled thereto, is not a prior conclusive determination that bars review of a subsequent final order granting allowances that are unjust and unlawful to parties who by law are not entitled thereto.[1]

III

Finally it is urged by respondent, Guaranty, that since petitioners do not challenge the jurisdiction of the State Court to foreclose the Utah Fuel stock and to adjudicate and define the liens of the respective bondholders, it must be held, as a necessary incident thereof, that the State Court had the power to fix allowances to the parties and their counsel and direct their payment out of the proceeds of sale of the Utah Fuel stock.

But the jurisdiction to grant allowances is an incidental one and is not required to permit a court to adjudicate the principal issues. That incidental jurisdiction must be denied when the exercise of that power has been reserved to itself by the Federal reorganization court.

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[1] An identical situation arose in *New York Trust Co. v. New York & Greenwood Lake Ry. Co.*, 156 F. 2d 701. There the Court in its final judgment of foreclosure reserved jurisdiction to pass on fees (pp. 702, 703). Upon subsequent application for allowances by the Trustee and its counsel, the Court denied allowances on the ground that it was without jurisdiction to award them, that the only appropriate source of payment was in the reorganization proceeding.

"The State court has full control over the litigation. But even as an incident thereto, it may not take action which involves the performance of functions which Congress has entrusted to the bankruptcy court" (*Brown* v. *Gerdes*, 321 U. S. 178, 186).

CONCLUSION

The instant petition presents substantial Federal questions that warrant and require review. For the reasons stated in our main brief and in this reply, the petition for certiorari should be granted.

Respectfully submitted,

PERCIVAL E. JACKSON,
Counsel for Petitioners.

Dated: August 20, 1951.